IN THE

Supreme Court of the U. S.

OCTOBER TERM, 1899.

No. 237.

S. DUFFIELD MITCHELL, Receiver in Bankruptcy of JOSEPH McD. SCOTT, doing business as J. McD. SCOTT & COMPANY, plaintiff, in Error,

vs.

JOHN C. McCLURE and W. REED & COMPANY.

No. 237
October Term,
1899.

Error to District Court of the United States for the Western District of Pennsylvania.

ARGUMENT FOR DEFENDANTS IN ERROR.

J. McD. Scott, the bankrupt, was a citizen of the State of Pennsylvania, residing within the Western District of Pennsylvania, and the defendants were also citizens of said State residing in the same district. So also was the receiver of the bankrupt.

The plaintiff in error's statement is substantially correct. The only question involved in this case is whether or not the District Court of the United States for the Western District of Pennsylvania had jurisdiction to entertain an action which was brought by the receiver of a bankrupt against a party in whose hands he claimed there were assets belonging to the bankrupt; the receiver, the bankrupt and the defendants all being citizens of Pennsylvania, resident in that district.

The section of the bankrupt law involved in this case is Section 23d, and is as follows:

a. "The United States Circuit Courts shall have jurisdiction of all controversies at law and in equity as distinguished from proceedings in bankruptcy between trustees as such and adverse claimants concerning the property acquired or claimed by the trustees, in the same manner and to the same extent only as

though bankruptcy proceedings had not been instituted and such controversies had been between the bankrupt and such adverse claimants."

b. "Suits by the trustee shall only be brought or prosecuted in the Courts where the bankrupt whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant."

A mere reading of this section would seem to make it clear that the action of replevin under consideration could not be maintained in the District Court of the United States because of the citizenship of the bankrupt and the defendants.

The plaintiff in error in the Court below sought to avoid this conclusion by making answer to the rule that he (the plaintiff) had taken the property upon the claim that the same had been conveyed by the bankrupt to defendants without consideration and in fraud of the Bankruptcy Act and of the rights of the creditors of such bankrupt, and that therefore no title had passed to defendants as against the receiver in bankruptcy.

It seem to us that this alleged fact can make no possible difference. In the enactment of the present bankrupt law congress undoubtedly intended

that the defendant in such a case as the present should not be dragged out of his own home into (in many cases) distant Courts of the United States, but that upon the contrary the trustee in bankruptcy should seek the defendant where the bankrupt himself would have had to seek him, namely, at his own residence.

The argument that because the bankrupt cannot maintain a suit to set aside as fraudulent a conveyance made by himself, therefore the provisions of Section 23d of the Bankrupt Law do not apply, is fallacious. Assuming that the bankrupt had brought an action of replevin in the State Courts, to meet the claim in the present case, he could not havs been defeated on the ground that the State Court had no jurisdiction. He could only have been prevented from recovery by reason of the fact that the Court would afford him no relief as against his own fraud. If he could have made a case without disclosing his fraud, in like manner the mouth of the defendant would be closed and he would not have been permitted to set up the fraud to defeat the plaintiff.

Burnett vs. Morris Mercantile Co., 91 Fed. Rep. 365.

The present question was fully discussed in Perkins vs. McCauley, et al., (98 Fed. Rep. 286). The syllabus of that case is as follows:

"Under the Bankruptcy Act of 1898, Section 23, B, providing that suits by the trustee in bankruptcy shall be brought or prosecuted only in those Courts where the bankrupt might have brought or prosecuted them if proceedings in bankruptcy had not been instituted the Court in Bankruptcy has no jurisdiction in a suit by a trustee to set aside the transfer of property made by the bankrupt and alleged to be in violation of the Act, either as a preference or as a fraudulent conveyance when the bankrupt or trustee and the defendant are citizens of the same State."

The provisions of the Bankrupt Acts of 1841 and 1867 as to the jurisdiction and powers given to Bankrupt Courts are not the same as those of the Act of 1898. They were very much broader. The effect of any decision under those Acts cannot avoid the plain, unmistakable language of the Act of 1898.

The argument drawn from the seventh clause of Chapter II. of the Bankrupt Act, to-wit, that the United States Courts are invested with such jurisdiction at law and in equity as will enable them to "cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided," has no bearing upon the question now before the Court. The trustee, of course,

is under the control of the Court which appointed him, and can be compelled by that Court to perform his duty. The words "except as herein otherwise provided" clearly relate to the words "determine controversies in relation thereto," and the after proviso is to be found in Section 23.

Hicks vs. Knost, 94 Fed. Rep., 627.

It is argued that Congress cannot compel the State Courts to litigate bankruptcy controversies, and that therefore the language of Section 23d must be twisted from its plain meaning. If the bankrupt had a right of action the fact that he was adjudged bankrupt would not induce a State Court to refuse to entertain a suit brought in his name for the use of his trustee in bankruptcy. If an individual parted with his property with intent to defraud his creditors, even if it be granted that he himself could not successfully maintain an action to recover possession of the property with which he had parted, it is a part of the common law of the land that his creditors could attack such transaction, and it is not to be presumed that any State should so fail in comity as to refuse to entertain an action for that purpose brought by a trustee in bankruptcy, who by the very fact of the adjudication in bankruptcy is vested with all the rights of the creditors for the recovery of their claims against their debtor. It is not at all clear, however, that in such case the State Courts would be without jurisdiction of a suit brought by a trustee in bankruptcy

to recover property which the bankrupt had parted with in fraud of his creditors and in violation of the Bankrupt Act.

The right to institute actions of that nature somewhere must necessarily exist in order to completely administer the estate of the bankrupt for the benefit of his creditors.

The Constitution of the United States, assented to by the several States, confers upon Congress the power to establish uniform laws on the subject of bankruptcy throughout the United States, and it also provides that full faith and credit shall be given in each State to the public acts, records and judicial proceedings of every other State. This latter provision was a necessary provision, because it expresses a mutual and common agreement between the States forming the Union. It was not necessary to make a like expression with reference to the credit to be given to public acts, records and judicial proceedings. That was necessarily implied.

Suppose a judgment was rendered in the United States Court, and that afterwards the parties to the action in which that judgment was rendered became residents of the same State, and it was desirable or necessary to enforce the judgment there: who would contend that an action upon such a judgment could only be brought in the Courts of the United States, or that, if brought in the State

Court, that that Court would not be bound to give full faith to the records of the Court of the United States in which judgment was entered? So in bankruptcy proceedings, when a man has been adjudged a bankrupt and a trustee has been appointed, it is necessarily implied by the record that that trustee, standing for the general body of creditors, has a right to enforce the claims of creditors against the estate of the bankrupt in whosoever's hands it may be found where the bankrupt has parted with that estate in violation of the provisions of the bankrupt law.

"A judgment in one State is conclusive between the parties in another State in the Federal Courts, and the defendants cannot plead any fact in bar which contradicts the record on which the suit was brought."

Insurance Co. vs. Harris, 97 U. S., 33.

But whether or not Congress had a right to require that the State Court shall entertain suits for the objects and purposes of the bankrupt law is immaterial. If Congress undertook to say that certain suits should only be brought in the Court in which the bankrupt could have brought them, and that happens to be a State Court, the remedy is by an amendment of the bankrupt law by Congress, and not through judicial interpolation.

Reference is made to the arbitration provision in Section 26. We fail to see in what way this section helps the contention of the plaintiff in error. It cannot be pretented that the Bankrupt Court can compel either the trustees or his adversary to consent to arbitration. Arbitration is a matter of mutual consent and being so consented to, is brought within the jurisdiction of the Court. And so under Clause "B" of Section 23, if the defendant had consented to a suit against him in the District Court it may well be that that Court would have had jurisdiction, but in this case he did not consent.

Another reason may be urged why Section 23d, in the absence of consent, does not confer jurisdiction, and that is this:

Section 25 of the Bankrupt Act defines the cases in which appeals may be taken, and an appeal in a case such as the present one is not provided for, and it is fair to assume that if such litigation in the District Court had been contemplated, the right to appeal would have been provided for.

It is said that the decision of the District Court in this case cannot be sustained, because Section 23d has no application to a right of action which accrues to the trustees solely by virtue of the bankrupt act; and it is contended that the alleged transfer by the bankrupt to defendants in error without consideration and with intent to defraud his credit-

ors, being an act of bankruptcy within the provisions of the act, is a cause of action created by the act itself, and therefore not within the meaning of Section 23d. It seems to us that this argument is more specious than sound. As we have already said, such a cause of action existed in favor of a creditor at common law. The well known statute of Elizabeth formed part of our common law. If any creditor saw fit to institute proceedings in bankruptcy within four months after the commission of the act, then the right of action which the creditors otherwise would have had, simply was transferred to the trustee in bankruptcy. Wherever receivers have been appointed it has always been recognized to be within the power of the receiver to follow assets fraudulently separated from the body of the estate.

On the whole, then, we contend that the decision of the District Court should be affirmed from the plain reading of the statute in question; that so far as it may be alleged that any inconvenience or delay may attend the administration of bankrupt estates by reason of the limitation of jurisdiction, that that is simply a matter for Congress to remedy, and it is no argument why the decision of the District Court should be reversed.

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